STAFF PAPER

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Project	**Business combination under common control**
	December meeting agenda for initial consideration

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Introduction

1. We will have an Emerging Economies Group (the EEG) meeting in December with an agenda for business combination under common control. Many respondents on *Agenda Consultation 2011* cited this project as a high priority. They believe that guidance is needed to clarify the accounting for common control transactions and reconcile the different characteristics of mergers and restructures around the world, because there is diversity in practice at present. We would benefit from a discussion of this issue by the EEG.

2. This issue is a very difficult area, and we will be seeking volunteersfrom the EEG to develop meeting materials.In this process, we need to lead them with the overall direction that specifies the scope, expected duration and timelineof the project so that the EEG's workwill be helpful to the future project for business combination under common control.

3. This paper summarisesthe agenda proposal and timetable with which the Board decided to add to its active agenda a project on common control transactions.

Project status & summary

4. In December 2007, the Board decided to add to its active agenda a project on common control transactions. Business combinations involving entities or businesses under common control are excluded from the scope of IFRS 3 *Business*

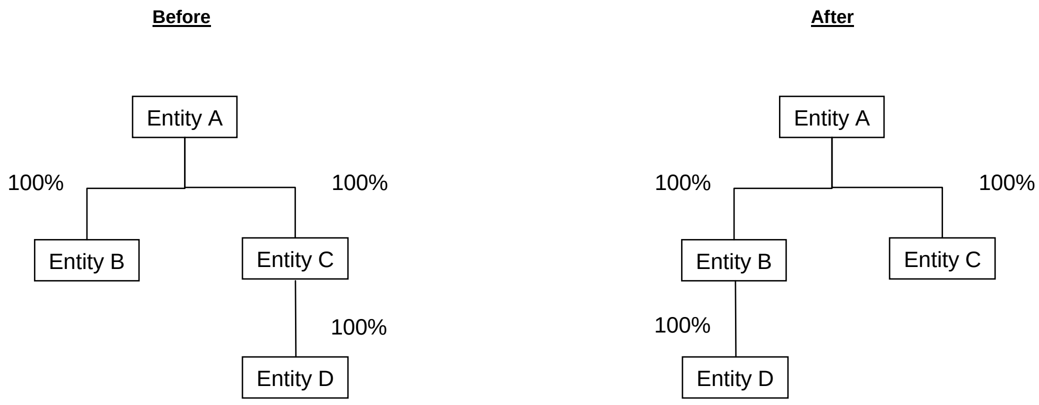
Combinations. As a consequence, practice diverges on the accounting for those transactions in the acquirer's consolidated and separate financial statements. The project examines the definition of common control and the methods of accounting for a business combination between entities or businesses under common control in the acquirer's consolidated and separate financial statements. Similar issues arise with respect to the accounting for demergers, such as the spin-off of a subsidiary or business. Therefore, the Board decided to include demergers in the scope of the project.

5. Since then, the staff had performed preliminary research on common control transactions and conducted field visits to obtain a better understanding of the conceptual and practical issues associated with those transactions.However, the project is currently paused due to resource constraints in staffing in 2009.

Background

6. A combination between entities or businesses under common control is a business combination where the controlling party before and after the transaction is the same. Those transactions arise often in the context of group restructurings. The party having common control might want to restructure its group for legal, tax or economic reasons. For example, a group restructuring might be undertaken to achieve a change in the tax base of a subsidiary, to enable the distribution of dividends, because of regulatory requirements or in preparation for a sale.

7. For example, assume that entity A owns all of the voting interest of entities B and C. Entity C owns all of the voting interest in entity D. Entity B acquires all voting interests in entity D from entity C.



8. The transaction is a combination between entities under common control because entities B, C and D are controlled by entity A before and after the transaction. This type of restructuring might be used in preparation, for example, for the sale by initial public offering of entity B and its subsidiaries (including entity D), commonly referred to as a spin-off transaction.

Issues

9. In the example in paragraphs 7 and 8, entity A's financial position remains unchanged before and after the transaction. Therefore, most constituents believe that if entity A prepares consolidated financial statements they should not be affected by a combination between entities or businesses under common control.

10. However, entity B would be required to present consolidated financial statements unless it meets certain conditions in accordance with paragraph 4 of IFRS 10*Consolidated Financial Statements*.If entity B is required to prepare consolidated financial statements, a question arises as to how the acquisition of entity D should be accounted for because paragraph 2(c) of IFRS 3 excludes combinations between entities or businesses under common control from the scope of the revised IFRS 3. The staff is aware of at least three accounting methods that are advocated in practice:

    (a) *Acquisition method*: The combination between entities or businesses under common control would be accounted for as if it were a business combination between unrelated parties. In the example, entity B would recognise entity D’s assets and liabilities at their acquisition date fair values.

(b) *Fresh-start method*: According to this method, all assets and liabilities of the newly formed group would be measured at their fair values. In the example, both, entity B’s and D’s assets and liabilities would be measured at their acquisition date fair values.

(c) *Pooling-of-interests method*: According to this view, the assets and liabilities of the involved parties would not be remeasured and rather entity D’s book values would be carried over in entity B’s financial statements. However, it is not clear which amounts should be carried over into entity B’s financial statements. Entity B could recognise entity D’s assets and liabilities at their carrying amounts in:

(i) entity A’s consolidated or separate financial statements;

(ii) entity C’s consolidated or separate financial statements; or

(iii) entity D’s individual financial statements.

11. In addition to the basic issue described in paragraphs 9 and 10, the staff has identified the following additional issues that could be addressed in a project on common control transactions:

(a) the project could revise the description of a combination between entities or businesses under common control to provide clearer guidance on when a transaction falls within the scope of IFRS 3;

(b) the project could undertake a comprehensive review of all new basisissues related to corporate restructurings; or

(c) the project could analyse all transactions between entities under common control, regardless of whether they represent a combination between entities or businesses under common control.

Timetable

12. In the 2007 agenda proposal, the staff recommended the following timetable:

Month	Topic
1 – 5	Preliminary research phase on combinations between entities or businesses under common control including an analysis of the fresh-start method
6	Project Outline and Education Session
7	The definition of a combination between entities under common control
8 – 9	Common control transactions in the acquirer's consolidated financial statements: - the acquisition method - the pooling-of-interests method
10	- the fresh-start method
11	Common control transactions in the acquirer's separate financial statements: - scope of IAS 27 - analysis of available accounting methods: (i) carrying amount (ii) fair value (iii) exchange amount
12	Cost/benefit analysis
13 – 15	Drafting of the discussion paper
16	Publication